

LFC Requester:

SUNNY LIU

AGENCY BILL ANALYSIS
2016 REGULAR SESSION

WITHIN 24 HOURS OF BILL POSTING, EMAIL ANALYSIS TO:

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and

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{Include the bill no. in the email subject line, e.g., HB2, and only attach one bill analysis and related documentation per email message}

SECTION I: GENERAL INFORMATION

{Indicate if analysis is on an original bill, amendment, substitute or a correction of a previous bill}

Check all that apply:

Original ☒ Amendment ☐
Correction ☐ Substitute ☐

Date January 22, 2016

Bill No: HJR 11

Sponsor: Rep. Patricia Roybal Caballero

Agency Code: 305

Short Limit Certain Interest Rates,CA

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Title:

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SECTION II: FISCAL IMPACT

APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Nonrecurring	Fund Affected
FY16	FY17		

(Parenthesis () Indicate Expenditure Decreases)

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Nonrecurring	Fund Affected
FY16	FY17	FY18		

(Parenthesis () Indicate Expenditure Decreases)

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY16	FY17	FY18	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total						

(Parenthesis () Indicate Expenditure Decreases)

Duplicates/Conflicts with/Companion to/Relates to:
Duplicates/Relates to Appropriation in the General Appropriation Act

SECTION III: NARRATIVE

BILL SUMMARY

This analysis is neither a formal Attorney General's Opinion nor an Attorney General's Advisory Letter. This is a staff analysis in response to an agency's, committee's, or legislator's request.

Synopsis:

HJR11 proposes an amendment to Article 20 of the Constitution of New Mexico.

HJR11 sets a maximum lawful rate of interest of 36% per year that may be charged or received for the extension of credit.

HJR11 excludes federally insured depository institutions and government issued bonds.

FISCAL IMPLICATIONS

Note: major assumptions underlying fiscal impact should be documented.

Note: if additional operating budget impact is estimated, assumptions and calculations should be reported in this section.

SIGNIFICANT ISSUES

HJR 11 allows the people of New Mexico to adopt a constitutional amendment to establish a definitive cap on usury. If enacted by the Legislature, the proposed amendment would be placed on the 2016 ballot. If adopted, the constitutional amendment would set usury boundaries for statutory laws that govern the State of New Mexico and affirm the right and obligation to protect New Mexicans—particularly those who are financially at risk—from predatory lending. The proposed amendment incorporates a basic standard of fairness in lending and is consistent with existing protections for consumers found at Article II, Section 21 of the New Mexico Constitution: “No person shall be imprisoned for debt in any civil action”; and Article II, Section 4: “all persons...have certain natural, inherent and inalienable rights, among which are the rights of acquiring, possessing and protecting property...”

Because of the history of the high cost lending market, consumer experts throughout the country advocate a 36% annual rate cap on the extension of credit as the most effective way to provide protections to financially at-risk borrowers and set viable limits to usury in the extension of credit. A 36% rate has been determined by consumer experts to permit reasonable priced loans to be made to borrowers who can afford to repay them while prohibiting destructive loans to borrowers who cannot. A 36% annual rate cap provides the framework for other legislative or

regulatory efforts to address the lending industry's marketing and loan practices that have had and continue to have an adverse impact on borrowers since deregulation occurred.

History of high cost lending in New Mexico

Prior to 1981, New Mexico law restricted interest rates on lending. Usury caps were "deregulated" in 1981 in response to inflation in the mortgage market place. The deregulation of all usury limitations resulted in the development of numerous loan products charging ever-increasing interest rates and marketed to New Mexicans with limited financial means. By the mid-2000's, the typical loans being offered in New Mexico included installment loans, payday loans, household goods loans and car title loans. Installment loans were offered either as simple interest loans or pre-computed interest loans. By 2005, common rates charged ranged from 80 to 600%. It was common for borrowers to roll their loan over several times without reducing the principal obligation due and owing. This rollover routine is linked to borrowers being trapped in a cycle of debt, paying back many times the small amounts financed on their loans over an extended period of time.

The payday loan products offered in New Mexico before 2007 were (at least nationally) short-term loans amortized over a 14-to-30-day term, and carried an average effective interest rate of 561%. Though the payday loans were written to be short-term loans with one-time payments, in practice they created much longer payment obligations. Prior to the 2007 payday loan reform provisions, the loans could be rolled over, renewed, or extended for an unlimited period of time. A rollover occurs when the borrower cannot retire the entirety of a payday loan obligation—i.e. the principal amount plus the interest and/or fee charged per \$100 borrowed—and allows the borrower to pay back only interest and fees while "rolling over" the entire principal amount financed into a "new" loan. The cause of the debtor's inability to pay off the principal owed was the cost of the credit – the high interest rates charged – and the borrower's limited financial resources and income.

The rollover routine was obviously the rule, rather than the exception, of payday lending, and reported abusive lending practices and the rates of interest charged focused legislative attention on payday loans, prompting the legislature to enact ameliorative measures set forth in Sections 58-15-31 through 39 of the Small Loan Act ("SLA" or the "Act").

The effort to reform payday lending in New Mexico reflects the legislature's overriding concern that high-cost loans can trap borrowers in a cycle of debt. Unfortunately, contrary to the prohibitions enacted in 2007 for payday loans, high cost lending has continued unabated, lenders have shifted their loan products to evade any consumer protections, rollovers continue, the no-cost repayment plan provided for payday loans is infrequently implemented, and consumers continue to be trapped in long-term, high cost indebtedness.

After 2007, many lenders shifted from offering payday loans to offering long-term installment loans, car titles loans, and other high cost loan products with rates averaging 350% per year with a reported interest rate high in excess of 2,000% per year. These loans include high cost interest rates, rollovers, and long-term indebtedness. Loan products currently being offered in New Mexico include payday loans, installment loans, car title loans, household goods loans and refund anticipation loans.

The Financial Institutions Division of the Department of Regulation and Licensing currently tracks data on payday loans and non-payday loan products with interest rates in excess of 175% per annum. The lending practices of installment lenders making loans with interest rates of less than 175% - for examples rates of 85% to 150% - are not currently tracked as a result of industry lobbying

efforts that succeeded in excluding this market from scrutiny. However, anecdotal information on this niche in the lending market is available.

Available FID data and reported consumer experience demonstrates that rollovers and long-term indebtedness continue to be a prevalent problem in the high cost market for loans with interest rates ranging from 85% to in-excess of 1,000% per year. On average 41% of non-payday loans are rollovers, renewals or refinanced loans. The debt trap is a function of the longer-term obligation that the multi-month installment loan products create, coupled with the inability of the borrower to repay the loan when due.

Problems in the high cost lending industry and its impact on military service members has also been the subject of scrutiny by the Department of Defense. In August 2006, the Department of Defense issued its "Report on Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents". ("Dept. of Defense Report") The Dept. of Defense Report reviewed short-term loans (payday, car title, and tax refund anticipation loans) and installment loans and found that "[p]redatory lending practices are prevalent and target military personnel..." The Dept. of Defense Report found that these lenders have characteristics in common, such as: targeting borrowers who are financially at risk; marketing products with high fees/interest rates; taking advantage of the borrower's inability to pay the loan in full when due and encouraging extensions through refinancing and loan flipping with additional fees and little or no payment of principal; and, evading usury limits or developing schemes to circumvent existing consumer protection laws. The Dept. of Defense recommended that:

"Lenders should be prohibited from directly or indirectly imposing, charging, or collecting rates in excess of 36 percent APR with regard to extensions of credit made to Service members and their families. This APR must include all cost elements associated with the extension of credit..."

In response, Congress enacted a 36% rate cap for short-term loans to the military and families for loans with terms less than 91 days, effective in 2007. However, lenders continue to target military personnel evading the 36% rate cap by offering longer-term loans (more than 91 days) to military personnel with triple digit rates. **New Mexico is 1 of 5 states that has been identified by the Dept. of Defense as having not made regulatory changes to promote enforcement of the DOD predatory lending regulations.**

Most recently, the New Mexico Supreme Court ruled in *State ex rel. King v. B & B Investment Group, Inc.*, 2014-NMSC-024, 329 P.3d 658, there was substantial evidence that subprime lenders took advantage of signature loan borrowers' lack of knowledge, experience, ability, or capacity in credit transactions, and the signature loans marketed by and originated by the lenders were grossly unfair and procedurally unconscionable under the New Mexico Unfair Practices Act (UPA) and under common law. The Court further ruled that installment loans bearing interest rates of 1,147.14% to 1,500.00% are substantively unconscionable under common law and the UPA, and were contrary to public policy as expressed in the UPA and other legislation. The Court declared that the unconscionable interest rates in the Defendants' loans were invalid terms and because the contracts were silent with respect to rates, the Court applied the statutory default interest rate of 15 % simple annual interest, (*see* NMSA 1978, § 56-8-3), to those loans for restitution purposes. Finally, the Supreme Court upheld the District Court's permanent injunction against the lender enjoining the lender from further engaging in its unconscionable lending practices.

PERFORMANCE IMPLICATIONS WITH ENACTING THIS BILL

ADMINISTRATIVE IMPLICATIONS WITH ENACTING THIS BILL

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP WITH BILLS INTRODUCED THIS SESSION

TECHNICAL ISSUES OR DRAFTING ERROR

OTHER SUBSTANTIVE LEGAL ISSUES

The Bill does **not** define the calculation of interest or that the 36% APR must include all cost elements associated with the extension of credit, e.g. periodic or non-periodic interest, periodic or non-periodic finance charges, ancillary products or services or other charges or fees incident to the extension of credit.

ALTERNATIVES TO ENACTING THIS BILL

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

High cost lenders will continue to charge financially strapped borrowers interest rates of 85% to 1500% or more; New Mexico families will expend \$100 million or more in interest and fees for these loans; borrowers will continue to be plagued by long-term indebtedness through rollovers and refinanced loans because the high cost prohibits borrowers from paying the loans off when due; and other adverse effects of the sub-prime (non-mortgage) lending market will continue unabated.

AMENDMENTS NEEDED TO IMPROVE THIS BILL

Define the calculation of interest or that the 36% APR must include all cost elements associated with the extension of credit including any periodic or non-periodic interest, any periodic or non-periodic finance charges, any ancillary products or services and any other charges or fees incident to the extension of credit.

PERFORMANCE IMPLICATIONS

ADMINISTRATIVE IMPLICATIONS

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

TECHNICAL ISSUES

OTHER SUBSTANTIVE ISSUES

ALTERNATIVES

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

Status quo.

AMENDMENTS